

Sales of canned computer software are taxable retail sales. See 86 Ill. Adm. Code 130.1935. (This is a GIL).

August 22, 2000

Dear Xxxxx:

This letter is in response to your letter received by our office on July 27, 2000 stating that it was a second request regarding a prior May 31, 2000. We apologize for the delay in responding to your inquiry. Our office did not receive your earlier letter. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120 subsections (b) and (c), which can be found at <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

In your letter, you have stated and made inquiry as follows:

Please note that our company is considering sales in your State. We would like to get a ruling from you on what components of our monthly support fee are taxable versus non-taxable elements. Please review our following descriptions and let me know on an individual basis the ruling on each aspect of our support program. All software mentioned is canned software and each element is separately stated on the monthly support billings. If you need further clarification on any of the descriptions below, please contact me at phone #####.

Customer Care: Software support services entailing assistance via telephone, fax and email help on the main computer software package. This will include instruction and database analysis.

Taxable _____ or Non-Taxable _____

Desktop Maintenance: Maintenance contract that keeps inter-office email/communications software running from year to year. This will also include software enhancements on this software package.

Taxable _____ or Non-Taxable _____

Hardware Maintenance: This component basically covers an annual hardware warranty contract.

Taxable _____ or Non-Taxable _____

NAME Software Enhancements: Ongoing software developments of NAME software that is released to customers on a semi-annual to annual basis. This is released in the form of a tangible data cartridge tape and mailed or couriered to customers.

Taxable _____ or Non-Taxable _____

Operating System Maintenance: This covers a partial support and enhancement contract to support their Computer's Operating System for Universe Databases.

Thank you for addressing our tax questions. This will assist greatly in the administration of our future needs.

We are unable to respond to your questions in the format provided. However, the following general information should answer your questions.

CANNED COMPUTER SOFTWARE

Sales of "canned" computer software are taxable retail sales in Illinois. See the enclosed copy of 86 Ill. Adm. Code 130.1935. If the computer software consists of custom computer programs, then the sales of such software are not taxable retail sales. See subsection (c) of Section 130.1935. Licenses of computer software are not taxable if they meet the requirements set out in part (1) of subsection (a) of Section 130.1935.

Custom computer programs or software are prepared to the special order of the customer. The selection of pre-written or canned programs assembled by vendors into software packages do not constitute custom software unless real and substantial changes are made to the programs or creation of program interfacing logic. See part (3) of subsection (c) of Section 130.1935.

COMPUTER SOFTWARE LICENSES

If transactions for the licensing of computer software meet all of the criteria provided in part (1) of subsection (a) of Section 130.1935, neither the transfer of the software or the subsequent software updates will be subject to Retailers' Occupation Tax.

A license of software is not a taxable retail sale if:

- A) it is evidenced by a written agreement signed by the licensor and the customer;
- B) it restricts the customer's duplication and use of the software;
- C) it prohibits the customer from licensing, sublicensing or transferring the software to a third party (except to a related party);

- D) the vendor will provide another copy at minimal or no charge if the customer loses or damages the software; and
- E) the customer must destroy or return all copies of the software to the vendor at the end of the license period.

Licenses of computer software are not taxable if they meet all of the criteria listed in part (1) of subsection (a) of Section 130.1935. However, item (D) of that part requires the license to contain a provision requiring the vendor to provide another copy at minimal or no charge if the customer loses or damages the software. The Department has deemed software license agreements to have met this criteria if the agreements do not contain a provision about the loss or damage of the software, but the vendors' records reflect that they have a policy of providing copies of software at minimal or no cost if the customers lose or destroy the software.

Item (E) of this part also requires a license to require a customer to destroy or return all copies of the software to the vendor at the end of the license period. The Department has also deemed perpetual license agreements to qualify for this criteria even though no provision is included in the agreements that requires the return or the destruction of the software.

SALE OF SOFTWARE UPDATES

Charges for updates of canned software are treated as sales of canned software. See subsection (b) of Section 130.1935. If the updates qualify as custom software under Section 130.1935(c), they may not be taxable.

MAINTENANCE AGREEMENTS

In general, maintenance agreements that cover computer software and hardware are treated the same as maintenance agreements for other types of tangible personal property. The taxability of maintenance agreements is dependent upon whether the charges for the agreements are included in the selling price of tangible personal property. If the charges for the maintenance agreements are included in the selling price of tangible personal property, those charges are part of the gross receipts of those retail transactions and are subject to tax. No tax is incurred on the maintenance services or parts when the repair or servicing is completed.

If maintenance agreements are sold separately from tangible personal property, the sale of those agreements are not taxable transactions. However, when maintenance services or parts are provided under those maintenance agreements, the service or repair companies will be acting as service providers under the Service Occupation Tax Act. The Service Occupation Tax Act provides that when service providers enter into agreements to provide maintenance services for a particular piece of equipment for a stated period of time at a predetermined fee, those service providers incur Use Tax based upon their cost price of tangible personal property transferred to the customers.

incident to the completion of the maintenance services. See part (3) of subsection (b) of the enclosed copy of 86 Ill. Adm. Code 140.301.

Please note that if a software maintenance agreement provides for updates or upgrades of canned software, and those updates or upgrades are not separately stated and taxed, the entire maintenance agreement is taxable as a sale of canned software.

TRAINING AND CONSULTING SERVICES

Assuming that the customer services provided, such as telephone support or other assistance through the use of fax or e-mail, do not require the transfer of tangible personal property to the recipients of those services, charges for such services are exempt if they are separately stated from the selling price of canned software. See Section 130.1935(b).

If computer software training or other support services are provided in conjunction with sales of custom computer software or licenses of computer software, the charges for that training are not subject to tax.

I hope this information is helpful. The Department of Revenue maintains a website, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b) described above.

Very truly yours,

Terry D. Charlton
Associate Counsel

TDC:msk
Enc.